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MEMORANDUM FOR: John Bushnell
National Security Council
Program Analysis
Room 481
OEOB 20506

SUBJECT : Relative Food Prices in Phnom Penh
and South Vietnam

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1. In response to your request of 6 December, we have put together the scant data on non-rice food prices for Phnom Penh and Saigon to determine whether there are any significant prospects for supply of Cambodian food needs from South Vietnam. Our results provide little basis for encouragement. In short, we find that most non-rice foods are relatively less expensive in Phnom Penh and that the dollar prices of these foods in Saigon are too high to encourage trade.

2. I would be the first to admit that more data are needed to allow a full inspection of this issue. In particular, we would like to see more detailed information on hard vegetables and dried foods. If any convenient and profitable trade proves possible, these sorts of commodities would be the least difficult to move from the relatively backward markets of South Vietnam to the even more-primitive storage in Phnom Penh.

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Problems in Non-Rice Food Trade Between
Cambodia and South Vietnam

An extremely thin data base for comparisons of non-rice food prices between Cambodia and South Vietnam precludes definitive statements on the prospects for trade flows. Nevertheless, readily available information provides insights on certain key facets of the problem. In the material that follows, attempts are made to: 1) clarify the nature of retail price increases in Phnom Penh for food items other than rice; 2) delineate the equivalent US dollar values and relative price structure for these commodities in Phnom Penh and South Vietnam; 3) discuss the related evidence on directions of trade from prevailing cross-border patterns of the recent past; and 4) itemize some of the impediments to trade beyond direct price problems.

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I. Available Price Indexes and the Nature of Cambodian Inflation

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1. [] has mistakenly set the rate of inflation in Phnom Penh at 275% for 1973. In reality, this is the October value in the government's cost-of-living index for the working class, and it therefore represents a price increase of 175% since the beginning of 1973. The food component for this index alone has increased about 220%.

2. There are a number of problems in using the official working class price index, which is -- unfortunately -- the most relevant available series.* Prices listed on the index are those found on the free market for a number of foodstuffs, housing, clothing, and other commodities. Foodstuffs are assigned a total weight of 60%, and rice carries a weight of 10%. A recent IMF study, however, estimates that a low-income family in Phnom Penh spends 60% to 80% of its income on rice. Moreover, most of this rice comes from direct government distribution outside the free markets. This means that the cost-of-living index is biased upward by the understatement of rice's importance in a situation in which more effort has been made to assure its steady supply than that of other commodities.

* There are two other price indexes compiled for the Phnom Penh area. The "middle class" index pertains to consumption by low level government workers and professionals. A "European class" index is for the elite of Phnom Penh.

3. These problems notwithstanding, it is apparent from the available components of the index that prices for non-rice foods on the free market have skyrocketed during 1973 (see Table 1). Although only fresh fish prices have actually risen more rapidly than those of free-market rice, any reasonable allowance for the officially distributed rice suggests that pork, lard, and rice wine have increased at least as rapidly as rice prices.* This clearly raises the question of whether external supply of these goods might not make a greater dent in consumer prices than would greater rice shipments.

* Assuming 75% of final sales are under the official program, the combined price increase for official and free-market sales during March-October would be about 200%. A similar adjustment applies to Saigon, where about 75% of retail sales presently come from government price-controlled outlets. The difference between official and free market prices is, however, much less than in Phnom Penh.

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Table 1

Food Price Index for the Working Class in Phnom Penh
March-October 1973

Riels Per Kilogram

| Commodity | Free-Market Prices in Riels | | Percent Increase | Index Weight (Full Budget = 1.0) |
|---------------------------|--------------------------------|---------|---------------------|-------------------------------------|
| | March | October | | |
| Number 2 Rice | 24.7 | 110.0 | 345 | .10 |
| Pork | 171.8 | 723.1 | 321 | .06 |
| Beef | 150.9 | 353.8 | 134 | .02 |
| Lard | 148.0 | 600.0 | 305 | .02 |
| Dried Fish | 180.0 | 450.0 | 150 | .09 |
| Fresh Fish | 61.8 | 311.5 | 404 | .05 |
| Duck Eggs (each) | 12.9 | 35.3 | 174 | .04 |
| Pickling Brine (a jar) | NA | 120.0 | NA | .02 |
| Vegetables | 24.0 | 30.0 | 25 | .06 |
| Bananas (a bunch) | NA | 73.8 | NA | .04 |
| Eggplant | NA | 104.6 | NA | .03 |
| Rice Wine (a litre) | 70.0 | 250.0 | 257 | .05 |
| Palm Sugar (one loaf) | NA | 8.0 | NA | .02 |

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II. Relative Prices for Phnom Penh and South Vietnam

4. The critical problem in determining the relative prices of non-rice foods in Phnom Penh and South Vietnam is the selection of an appropriate exchange rate. No single approach to this problem is wholly satisfactory. Accordingly, we have taken three different tacks to develop a rough sense of what goods might flow in either direction. Two of these make use of dollar cross-rates and the third ignores money exchange problems by looking directly at internal relative prices.*

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5. The first approach is to accept the judgment of [] that prevailing official rates in late 1973 were probably realistic for commodity trade in the border areas.** This leads to the specific price comparisons shown in Table 2. These figures suggest that in

* The commodities shown in Tables 2, 3 and 4 account for approximately 80% of Phnom Penh's and 60% of Saigon's food price indexes.

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Table 2
Comparisons of Retail Prices at
Official Exchange Rates a/

| <u>Commodity</u> | <u>Dollars per Kilogram</u> | | | |
|-----------------------------------|-----------------------------|-------------------|----------------|-------------------|
| | <u>March</u> | | <u>October</u> | |
| | <u>Saigon</u> | <u>Phnom Penh</u> | <u>Saigon</u> | <u>Phnom Penh</u> |
| Rice | 0.16 | 0.11 | 0.26 | 0.36 |
| Beef | 1.11 | 0.66 | 1.73 | 1.17 |
| Pork | 1.52 | 0.75 | 1.92 | 2.39 |
| Fresh Fish | 0.74 | 0.27 | 1.02 | 1.03 |
| Dried Fish | 0.52 | 0.78 | 0.66 <u>b/</u> | 1.49 |
| Duck Eggs (each) | 0.04 | 0.06 | 0.05 | 0.12 |
| Bananas (per bunch) | 0.14 | 0.13 | 0.19 <u>b/</u> | 0.24 |
| Vegetables | 0.11 | 0.10 | 0.11 | 0.10 |
| Rice Wine | 0.24 | 0.30 | 0.40 <u>b/</u> | 0.83 |
| Averages <u>c/</u> | | | | |
| All Items (% increase) | 0.67 | 0.26 | 0.90 (+34%) | 0.70 (+169%) |
| Excluding Rice (% increase) | 0.94 | 0.42 | 1.24 (+32%) | 1.03 (+145%) |

a/ Official local currency/dollar rates used for conversion were, for Saigon: the effective export rate of 575 in March and October; for Phnom Penh: March 230 and October 302.

b/ September

c/ Weighted averages. For Saigon, rice one third; for Phnom Penh, rice one half. The remaining items are weighted according to their significance in the respective cities' indexes. The higher average prices in Saigon in October are due largely to the much greater weight applied to pork (40% of non-rice food purchases) than in Phnom Penh (16%). Applying the same weights to non-rice items in both cities produces a slightly higher average price for non-rice food commodities in Phnom Penh than in Saigon.

early 1973 food prices in Phnom Penh were about half those prevailing in Saigon. Despite a more-than-doubling of Phnom Penh food prices during April-October, the commodity sample indicates that overall food prices in Phnom Penh are still somewhat lower than in Saigon. The differential has narrowed considerably, however, and for some commodities an incentive to sell to Phnom Penh markets may now exist.

6. Another approach is to adjust the riel based on comparative price changes and reasonable estimates of piaster exchange rates during January 1970 - October 1973. For this purpose, we assume that the official Cambodian exchange rate of 55 riels = US \$1 and an estimated 335 piasters = US \$1 for South Vietnam are best for January 1970. These rates are borne out by our other analytic experience in the two countries, and by inspection of prevailing black market and Hong Kong rates. When drawn forward at the appropriate working class price indexes for Phnom Penh and consumer price index for Saigon, they produce exchange rates that result in the commodity prices shown in Table 3. Despite some narrowing of relative food prices between the two capital cities, the more rapid depreciation of the riel provides even less economic rationale for expanded trade than before.

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Table 3

Comparisons of Retail Food Prices
at Adjusted Exchange Rates a/

| <u>Commodity</u> | <u>Dollars per Kilogram</u> | |
|--------------------|-----------------------------|-------------------|
| | <u>March</u> | <u>October</u> |
| | <u>Saigon</u> | <u>Phnom Penh</u> |
| Rice | 0.16 | 0.14 |
| Beef | 1.11 | 0.82 |
| Pork | 1.52 | 0.93 |
| Fresh Fish | 0.74 | 0.34 |
| Dried Fish | 0.52 | 0.97 |
| Eggs | 0.04 | 0.07 |
| Bananas | 0.14 | 0.16 |
| Vegetables | 0.11 | 0.13 |
| Rice Wine | 0.24 | 0.38 |
| <u>Averages c/</u> | | |
| All Items | 0.67 | 0.32 |
| Excluding Rice | 0.94 | 0.52 |

a/ Cambodia's foreign exchange rate was depreciated by its rate of inflation relative to South Vietnam's. The effective rates used were for Saigon: 575 in both March and October; for Phnom Penh: March 185 and October 441. Piaster/Riel ratios thus rise from 0.32 in March to 0.77 in October.

b/ September

c/ See footnote C, Table 2. The same weighting methodology was employed.

7. Finally, ignoring exchange rates and simply looking at the relative price structure within the two countries permits some judgments on the direction of commodity flows. The appropriate relatives are expressed in terms of the price of a kilogram of rice in Table 4. Remarkably, this series only drives home more strongly the impression that most non-rice foods are relatively less expensive in Phnom Penh than in Saigon, and that price changes since early 1973 have reinforced this pattern. Exceptions to the former point are dried fish, duck eggs, and rice wine. Even in these instances relative price incentives for South Vietnam declined during March-October as a result of different rates of price change.

8. It thus appears that based on relative prices alone, existing rates of exchange between riels and piasters provide very little incentive for a greater flow of foodstuffs from South Vietnam to Phnom Penh. In order to provide a 25% price differential between Phnom Penh and Saigon, the present riel/piaster ratio of between 0.5 and 0.8 would have to be adjusted to around 0.3. This would involve a substantial revaluation of the riel relative to the piaster. At the present piaster/dollar exchange rate of 575:1, for example, the riel/dollar rate would have to be adjusted to about 190:1.

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Table 4

Phnom Penh and Saigon Food Prices
Expressed in Terms of Rice*

| Commodity | March 1973 | | | October 1973 | | |
|------------|------------------------|-------------------|--|------------------------|-------------------|--|
| | <u>Price Relatives</u> | | <u>Ratios of</u> <u>Price Relatives</u> | <u>Price Relatives</u> | | <u>Ratios of</u> <u>Price Relatives</u> |
| | <u>Saigon</u> | <u>Phnom Penh</u> | | <u>Saigon</u> | <u>Phnom Penh</u> | |
| Beef | 7.05 | 6.00 | 1.18 | 6.79 | 3.25 | 2.09 |
| Pork | 9.68 | 6.82 | 1.42 | 7.50 | 6.64 | 1.13 |
| Fresh Fish | 4.74 | 2.45 | 1.93 | 4.00 | 2.86 | 1.40 |
| Dried Fish | 3.32 | 7.09 | 0.47 | 2.57 | 4.14 | 0.62 |
| Duck Eggs | 0.26 | 0.55 | 0.47 | 0.21 | 0.33 | 0.64 |
| Pananas | 0.89 | 1.18 | 0.75 | 0.75 | 0.67 | 1.12 |
| Vegetables | 0.68 | 0.91 | 0.75 | 0.43 | 0.28 | 1.54 |
| Rice Wine | 1.53 | 2.73 | 0.56 | 1.57 | 2.31 | 0.68 |
| All Items | 6.00 | 3.82 | 1.57 | 4.86 | 2.86 | 1.70 |

The Price Relatives columns express the prices of non-rice foodstuffs in terms of rice. For example, the first entry of 7.05 indicates that in Saigon the price of a kilogram of beef is 7.05 times as great as the price of a kilogram of rice; in Phnom Penh the same quantity of beef in March cost 6 times as much as the same quantity of rice. The columns showing Ratios of Price Relatives express the price relatives in ratio form: Saigon/Phnom Penh. In the first entry then, $7.05/6 = 1.18$. When the ratio is greater than 1.0 the particular commodity under question is relatively more expensive in Saigon.

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III. Cross-Border Trade Patterns

9. Trade across the Cambodia/South Vietnam border, though not significant on a national scale, traditionally has played an important role in the local economies of the border provinces. At various points, the movement of food and goods has been highly visible, particularly at major trading points near the border in Tay Ninh Province (GVN MR 3) and Chau Doc and Kien Phong provinces in the Mekong Delta. A large portion of the cross-border trade has been conducted on a barter basis by myriad small merchants, and has generally been confined to a relatively small geographical zone. Although trade in these areas has been conducted on a quasi-legal basis, commodities have moved relatively freely with government interference limited to a traditional system of bribes at official checkpoints. With the exception of some handicraft and manufactured items, very few commodities ever reached the capitals of either country.

10. A major implication of the cross-border trade has been its use as a source of supply for VC/NVA forces operating in Cambodia and the southern half of South Vietnam. Communist procurement procedures since the beginning of the war have been predicated on the availability of food and goods in market places in the border areas. Before the outbreak of hostilities in Cambodia, major trade flows to the VC/NVA were into South Vietnam from Cambodia, where prices for various key goods were

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lower and supplies were more abundant. Growth of the Khmer insurgency movement has, however, affected earlier procurement patterns of the VC/NVA forces. The flow of goods appears now to have reversed and a larger share of the Communist food requirements are being met in South Vietnam. Several factors account for this phenomenon:

--prices for certain major foods have not increased as fast in South Vietnam as in Cambodia

--since the January ceasefire, the VC/NVA have reorganized procurement somewhat to rely more on the open market

--there has been a relatively abundant rice harvest in South Vietnam this year

--the Khmer Communists, who now have a sizable rice and food requirement, have competed more vigorously to ensure their own supplies

--large numbers of VC/NVA main force units have been moved from Cambodia back into South Vietnam.

11. Despite the large commodity flows in support of military activities, however, resumption of significant civilian cross-border trading activities does not seem likely in the near future. The types of goods observed moving from South Vietnam to Cambodia during 1973 include rice, flour, salt, nuoc mam, cloth in bolts, gasoline and diesel fuel.

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The GVN in mid-1973, however, took strong measures to cut off cross-border trade. The GVN assumed -- with probable validity -- that all such trade was destined for Communist hands. To date, the GVN program appears to have reduced the cross-border movement of goods considerably, although some no doubt still exists. Communist forces, too, are reported to have recently taken measures to stop intercountry movements of food and goods. The VC/NVA in South Vietnam -- experiencing tight supply conditions -- are reluctant to allow goods to flow into Cambodia. Similarly, the Khmer Communists have placed trade restrictions on commodities in their areas. Thus, economic incentives for trade in the border areas are being overridden by military logistic considerations.

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IV. Further Problems in Food Trade

12. Beyond the obvious impediments posed by security conditions and GVN or VC/NVA efforts to seal off certain areas, there are other serious uncertainties surrounding costs in moving goods to Phnom Penh and assuring their steady availability to consumers. First, delivery costs would vary considerably depending on the nature of the goods. Second, some of the food items in which inflation has been most rapid are perishable, and both refrigerated shipment and storage would be necessary to ensure their sale in any significant quantities. Related to this is the question of whether different marketing or distribution facilities might be necessary for the Vietnamese goods because of the form in which they arrived. Finally, the sorts of goods most needed in Phnom Penh are ones for which there is little large-volume internal marketing in South Vietnam,* and it is probable that they could not be quickly assembled for export.

* In this -- and other aspects -- sales of South Vietnamese foods to Phnom Penh are no different than their exports to any other part of the world.

V. Major Conclusions

13. Even before transport and other costs are added on, it would appear that few non-rice foods could profitably be shipped from Saigon to Phnom Penh. Both absolute and relative price analyses suggest opportunities only for such items as dried fish, duck eggs, and rice wine. Recent developments in the traditional cross-border trade provide no encouragement; indeed, the increasing tendency of the opposing military forces to seal off their areas and lock in needed commodities works against maintenance of earlier trading patterns. Finally, even allowing minimal security obstacles, problems in shipping, marketing, and storage for the sorts of commodities most needed in Phnom Penh would require large markups to move the goods up from South Vietnam.